

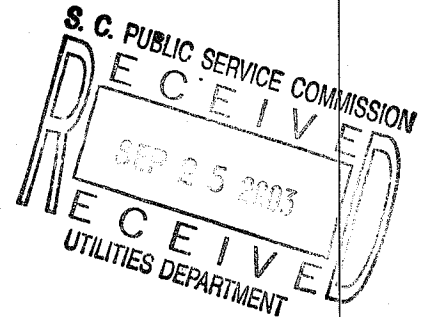
ORIGINAL

POSTED
09/25/03

Lake Princeton Water Company

Application for Increase in Rates and Charges

Docket No. 2003-213-W



HEARING DATE

October 9, 2003

***Testimony of
Jacqueline R. Cherry
Audit Department***

Public Service Commission of South Carolina

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TESTIMONY OF JACQUELINE R. CHERRY

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FOR

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THE PUBLIC SERVICE COMMISSION OF SOUTH CAROLINA

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DOCKET NO. 2003-213-W

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IN RE: LAKE PRINCETON WATER COMPANY

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**Q. PLEASE STATE FOR THE RECORD, YOUR NAME, BUSINESS ADDRESS
AND POSITION WITH THE PUBLIC SERVICE COMMISSION OF SOUTH
CAROLINA.**

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A. My name is Jacqueline R. Cherry. My business address is 101 Executive Center
Drive, Columbia, South Carolina. I am employed by the Public Service Commission
of South Carolina, Audit Department, as an auditor.

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**Q. PLEASE STATE YOUR EDUCATIONAL BACKGROUND AND YOUR
BUSINESS EXPERIENCE.**

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A. I received a B.S. Degree in Business Administration, with a major in Accounting,
from Johnson C. Smith University in 1976. I was employed by this Commission in
February 1979, and have participated in cases involving gas, electric, telephone, and
water and wastewater utilities.

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**Q. WHAT IS THE PURPOSE OF YOUR TESTIMONY IN THIS PROCEEDING
CONCERNING LAKE PRINCETON WATER COMPANY?**

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1 A. The purpose of my testimony is to set forth, in summary form, the Staff's findings
2 and recommendations resulting from our review of the Company's application in this
3 docket. These findings and recommendations are set forth below and in the report of
4 the Audit Department with attached exhibits.

5 **Q. I SHOW YOU THIS DOCUMENT. WOULD YOU PLEASE IDENTIFY IT?**

6 A. This is the "Public Service Commission of South Carolina, Commission Staff
7 Report, Lake Princeton Water Company, Docket No. 2003-213-W, Application for
8 Rate Increase".

9 **Q. DID YOU PREPARE, OR CAUSE TO BE PREPARED UNDER YOUR**
10 **DIRECTION AND SUPERVISION, A PORTION OF THIS DOCUMENT?**

11 A. Yes, with the exception of that portion which is tabbed Utilities Department, I
12 prepared the report, with assistance from the Audit Department Staff.

13 **Q. (MARK FOR IDENTIFICATION). NOW WOULD YOU EXPLAIN THE**
14 **CONTENTS OF THIS REPORT?**

15 A. As outlined in the Index of Staff's report, the first three pages contain the report
16 analysis. The remaining pages consist of exhibits that were prepared to show various
17 aspects of the Company's operations and financial position. The major portion of my
18 testimony will refer to Audit Exhibit A, Operating Experience and Operating Margin,
19 as shown on page 4 of the Staff's report. Staff prepared this exhibit in compliance
20 with the Commission's standard procedures for Water and Wastewater utility rate
21 cases.

22 **Q. PLEASE EXPLAIN THE FORMAT OF AUDIT EXHIBIT A.**

1 A. Column (1) shows the Company's per book balances as of December 31, 2002. Staff
2 verified the per book balances to the Company's books and records.

3 Column (2) shows the Staff's accounting and pro forma adjustments designed to
4 normalize the Company's per book operations.

5 Column (3) shows Staff's computation of the Company's normalized test year prior
6 to giving effect for the proposed increase.

7 Column (4) shows the Staff's adjustments for the proposed increase as furnished by
8 the Utilities Department and the adjustments associated with the additional revenue.

9 Column (5) shows the Staff's computation of the normalized test year after the
10 accounting and pro forma adjustments, and the effect of the proposed increase and its
11 associated adjustments.

12 Q. **WOULD YOU PLEASE ELABORATE ON THE CALCULATIONS IN**
13 **EXHIBIT A?**

14 A. Shown in column (1) is the per book operating experience of the Company's water
15 operations. Staff computed Total Income (Loss) for Return of (\$1,803) based on
16 operating revenues of \$1,879 less operating expenses of \$3,682. Total Income (Loss)
17 for Return of (\$1,803) and Operating Revenues of \$1,879 produced an Operating
18 Margin of (95.96%). In column (2), Staff's accounting and pro forma adjustments
19 were designed to normalize the Company's test year operations. A description of
20 each adjustment is contained in Audit Exhibit A-1. In column (3), the accounting
21 and pro forma adjustments decreased Total Income (Loss) for Return to (\$465) and
22 increased the Operating Margin to (19.85%). Column (4) shows the effect of the

proposed increase as computed by the Utilities and Audit Departments. These adjustments are detailed in Exhibit A-1 of the report. Column (5) shows per book operations as adjusted to normalize the test year and after the proposed increase is added to as adjusted revenues. As a result, Total Income (Loss) for Return of \$958 was computed by the Staff. Such income was based on operating revenues of \$4,025 less operating expenses of \$3,067. An Operating Margin of 23.80% was computed using the Total Income (Loss) for Return of \$958 and operating revenues of \$4,025. In this exhibit, Customer Growth was \$-0- because the number of customers (11 customers) did not change during the test year. The number of customers was provided by Staff's Utilities Department.

Q. WOULD YOU PLEASE EXPLAIN THE ADJUSTMENTS IN EXHIBIT A-1?

A. Yes, the adjustments are as follows:

Adj. #1—Water Service Revenue--\$463 – (Line #1) The Utilities Staff proposes to annualize water operating revenues by an adjustment of **\$463** to reflect the billed revenue for the test year. The Company proposes to annualize water operating revenues by an adjustment of **\$464** to reflect the billed revenue for the test year. This adjustment includes billing the Company's owners for water service for the test year.

Adj. #2 – Operation & Maint. Expense—(\$520) – (Line #2) Per the Company's application, the Company proposed an estimated increase in electricity expense by \$52. The Staff reviewed electricity bills and could not verify that this expense will increase. Therefore, the Staff did not accept the proposed adjustment by the

1 Company. The Staff does not consider the adjustment to be known and measurable
2 at this time.

3 (Line #3) The Staff made an adjustment of **(\$182)** to eliminate test year electricity
4 expenses that were not related to Company operations. This type of expense is
5 considered non-allowable for ratemaking purposes.

6 (Line #4) The Staff proposes to eliminate the test year DHEC surcharge expense of
7 **(\$150)**. The Company, in its application, reflected it as an on-going expense.
8 DHEC's Safe Drinking Water Act annual surcharge expense is recoverable by the
9 Company, as a separate item, in its water service customer billings. It comes under
10 DHEC's jurisdiction. The Company did not include this surcharge in its proposed
11 rates.

12 (Line #5) The Company proposed to include Officers & Maintenance Salaries
13 expense of \$1,000. This \$1,000 salary would be for the Company's President,
14 Douglas H. Kinard, who also performs maintenance duties for the Company. Mr.
15 Kinard has been receiving free water service for services rendered in place of a
16 salary. The Company did not pay salaries to Mr. Kinard or to its
17 Bookkeeper/Secretary during the test year. Mr. Kinard stated that he spends
18 approximately 8 to 10 hours per month performing his duties. Such duties include:
19 Signing off on each PSC & DHEC document as prepared by the Company's
20 Secretary/Treasurer; Checking pumps and the water supply quarterly; Installing new
21 meters as needed; Fixing all leaks; Checking pumps and water lines more often in
22 severe cold weather; Handling complaints; Checking pressure on pumps daily; and

1 Interacting with customers. The Staff reviewed the duties of Mr. Kinard and did not
2 consider the requested amount to be unreasonable based on the duties performed.
3 Therefore, the Staff accepted the salary adjustment proposed by the Company of
4 **\$1,000.**

5 (Line #6) The Company proposed an increase to \$120 for the Water Meter Reading
6 and Maintenance labor expense. Terry Black, the spouse of Sarah K. Black, one of
7 the Company's owners, performs this function. His duties include: Reading meters
8 each month; Checking for leaks in residences and water lines by checking meters;
9 Cleaning dirt out of meters each month; Cutting weeds and brush to get to the meters;
10 and Killing ants and other insects. Based on the duties performed, the Staff did not
11 consider the requested salary to be unreasonable. During the test year, \$60 was paid
12 for this expense. Therefore, both the Company and the Staff increased this expense
13 by **\$60.**

14 (Line #7) The Staff and the Company propose to reduce pump repairs expense for the
15 test year by **(\$900)** for the purchase of a new pump. Staff is of the opinion that the
16 expense should be capitalized for ratemaking purposes. It should be noted that the
17 Company proposed depreciation expense on this purchase. (See Line Number 16,
18 Audit Exhibit A-1, Page 6 of 7.)

19 (Line #8) The Staff and the Company propose to reduce the materials expense by
20 **(\$136)** for two meters with meter boxes purchased during the test year. Staff is of the
21 opinion that the expense should be capitalized for ratemaking purposes.

1 (Line #9) The Staff and the Company propose to eliminate a test year equipment
2 expense (a refrigerator) for **(\$212)** that was not related to Company operations. This
3 type of expense, pertaining to non-regulated operations, is considered non-allowable
4 for ratemaking purposes.

5 (Line #10) The Company proposed to increase expenses by \$318 for an Emergency
6 Fund equal to 10% of the Company's proposed expenses. The Company's prefiled
7 testimony has not addressed a need for such a fund and it is based on an arbitrary
8 10% of proposed expenses. It is not a known and measurable expense. Staff did not
9 adjust expenses for this estimate.

10 **Adj. #3—Administrative & General Expense--\$866--**(Line #11) The Company
11 and the Staff proposed an increase in professional services expense to \$100 based on
12 an increase in the accounting service fee for the preparation of the Company's
13 Annual Financial Reports. Staff verified the increase in the cost from \$50 to \$100.
14 The Staff's adjustment is based on a known and measurable change in test year
15 expenses. Therefore, Staff increased this expense by **\$50**.

16 (Line #12) The Company proposed a Bookkeeper/Secretary Salary expense of \$800.
17 This \$800 salary would be for the Company's Secretary/Treasurer, Sarah K. Black,
18 who performs administrative duties for the Company. Such duties include:
19 Calculating water usage on each meter each month; Calculating monthly billings;
20 Printing notices, envelopes and mailings; Collecting and recording payments that are
21 made; Preparing the PSC Annual Report; Preparing the DHEC Annual Report;
22 Handling complaints; Making bank deposits as needed; Balancing the Company

1 checkbook monthly; Paying all bills, taxes and fees; and Setting up new customer
2 accounts. As mentioned previously, Mrs. Black has been receiving free water service
3 for services rendered in place of a salary because the Company could not afford
4 salaries. Based on the duties performed by Mrs. Black, the Staff did not consider the
5 requested salary of \$800 to be unreasonable. It should be noted that in Mrs. Black's
6 prefiled testimony, dated September 1, 2003, she stated that her salary should be at
7 least \$600 annually. The Staff accepted the adjustment to include the salary
8 proposed by the Company of \$800, as contained in its application.

9 (Line #13) The Company proposed an estimated increase of \$17 for postage and
10 office supplies expenses. The Staff did not include such an increase in expenses
11 because it is not known and measurable at this time.

12 (Line #14) The Company proposed an estimated 20% increase to the Company's
13 proposed expenses as a 'Profit to the Company' in the amount of \$637. The Staff did
14 not accept the adjustment because "Profit" is not an expense item. Profit or (Loss) is
15 reflected on the "Net Operating Income or (Loss)" line of Staff's Exhibit A.

16 (Line #15) Staff proposes to adjust expenses by \$16 to reflect, on a normalized basis,
17 the costs of \$47 associated with the current rate case amortized over a three-year
18 period ($\$47 / 3 \text{ Years} = \16). Staff used a three-year rate case amortization period
19 because the Company did not have enough "rate case history" for Staff to compute
20 an average of the periods of time between the Company's rate cases. The Company
21 has only had one previous case before this Commission, a 1984 rate case for its
22 present rates.

1 **Adj. #4—Depreciation Expense--\$95--**(Line #16) Staff proposes to adjust expenses
2 by \$90 to reflect the depreciation expense associated with a pump purchased during
3 the test year (referred to in Adj. #2-- Line #7). The Utilities Staff provided the Audit
4 Staff with the Depreciation Rate for this proposed Plant item. The Staff agreed with
5 the Company's proposed depreciation expense on this item, also for \$90.

6 (Line #17) The Staff proposes to adjust expenses by \$5 to reflect the depreciation
7 expense associated with meters and meter boxes purchased during the test year
8 (referred to in Adj. #2-- Line #8). The Utilities Staff provided the Audit Staff with
9 the Depreciation Rate for this Plant item.

10 **Adj. #5—Taxes Other Than Income—(\$1,316)**—(Line #18) The Staff and the
11 Company propose to reduce test year property taxes to reflect the elimination of
12 property taxes that were not related to Company operations. This type of expense,
13 pertaining to non-regulated operations, is considered non-allowable for ratemaking
14 purposes. The Staff adjusted this expense by **(\$1,316)**. The Company's adjustment
15 totaled (\$1,317).

16 **Adj. #6—Water Service Revenue--\$1,683**—(Line #19) The Utilities Department
17 Staff computed the total effect of the proposed increase to be **\$1,683**. The Company
18 proposed an increase of \$1,821 in additional revenues.

19 **Adj. #7—Taxes Other Than Income--\$32**—(Line #19) The Company did not
20 have any gross receipts taxes per books. Therefore, the Staff proposes to compute
21 gross receipts taxes using the total proposed revenue of \$4,025 on an After the
22 Proposed Increase basis. The Staff applied the most current gross receipts tax rate

1 of 0.0080610529 to the amount of \$4,025, which produced a gross receipts tax
2 adjustment of \$32. The Company was not assessed a 2002 PSC Gross Receipts
3 Tax Fee because the revenue was less than \$4,000. However, it is Staff's opinion
4 that if the proposed revenue total of \$4,025 is approved, on a going forward basis,
5 the Company would be assessed a gross receipts tax.

6 Adj. #8—Income Taxes--\$228—(Line #19) To account for the effect of the
7 proposed increase, Staff computed income taxes of \$228 associated with the
8 additional revenues. Staff used a 5% tax rate to compute state income taxes and a
9 15% tax rate to compute federal income taxes.

10 **Q. WOULD YOU PLEASE ELABORATE ON THE REMAINING EXHIBITS?**

11 **A.** Exhibit A-2 shows the Depreciation Expense adjustments. Exhibit A-3 shows Staff's
12 Computation of Income Taxes after the accounting and pro forma adjustments, and
13 after the proposed increase. Exhibit A-4 shows the Income Statement per the
14 Company's Application for the Test Year Ended December 31, 2002. Exhibit A-5
15 shows Staff's Alternate Revenue Requirements reflecting various revenues after a
16 proposed increase and based on a range of operating margins between 0% and
17 23.80%.

18 **Q. WHAT IS THE RESULTANT OPERATING MARGIN FROM THE RATES**
19 **BEING REQUESTED IN THIS CASE?**

20 **A.** As calculated by Staff, the resultant Operating Margin would be 23.80% for the
21 Company's water operations.

22 **Q. DOES THIS CONCLUDE YOUR TESTIMONY?**

1 A. Yes, it does.